LEGISLATIVE SERVICES AGENCY
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FISCAL IMPACT STATEMENT

LS 6364
BILL NUMBER: SB 599

NOTE PREPARED: Jan 17, 2005
BILL AMENDED:

SUBJECT: Property Tax Credit Based on Income.

FIRST AUTHOR: Sen. Kruse
FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: X **GENERAL**
X **DEDICATED**
FEDERAL

IMPACT: State & Local

Summary of Legislation: The bill provides a Property Tax credit equal to the amount by which Property Tax on a homestead exceeds 10% of the owner's three year average Gross Income. The bill requires a credit application that includes income information to be filed with the County Auditor. It also applies current confidentiality requirements to income information and other financial information received by the County Auditor.

Effective Date: July 1, 2005.

Explanation of State Expenditures: *Summary:* It is estimated that the proposed property tax credit could potentially increase state expense for PTRC and homestead credit payments by $10 M in FY 2007 (partial year) and $30 M per year in subsequent years.

Background: The state pays Property Tax Replacement Credits (PTRC) in the amount of 60% of school general fund levies attributable to all property and 20% of the portion of all operating levies (including the remaining 40% of the school GF levy) that are attributable to real property and non-business personal property. Homestead Credits are paid by the state in the amount of 20% of the net property tax due for qualifying funds on owner-occupied residences.

The higher property tax rates caused by the bill, as explained in *Explanation of Local Revenues*, would cause the gross charged (or abstract) levy to increase. Since PTRC and homestead credit payments are calculated using the gross abstract levy, the state's payments for these credits would increase under the proposal. The increase in state expense for these credits is estimated at $10 M in FY 2007 (partial year) and $30 M per year in years following.

PTRC and Homestead Credits are paid from the Property Tax Replacement Fund (PTRF). These credits are paid from the state General Fund if insufficient balances are available in the PTRF.

Explanation of State Revenues:

Explanation of Local Expenditures:

Explanation of Local Revenues: *Summary:* The bill establishes a property tax credit for homestead owners to be applied against the net property tax bill. The credit would first apply to 2006 Pay 2007 property taxes. It is estimated that credits claimed could potentially total about $102 M annually beginning with Pay 2007 property taxes. However, total credits could potentially decline beginning with Pay 2009 taxes by about 0.3% annually based on current forecasts suggesting that growth in income exceeds growth in net property taxes on homesteads.

Overall, about $30 M of the $102 M credit would be shifted to the state in the form of higher PTRC and homestead credits and the majority of the remaining $72 M credit will be shifted from homeowners to all property owners. The remainder would be lost revenue in the rate-controlled funds such as cumulative building and capital projects funds

Background: Property Tax Credit: The property tax credit is equal to the greater of either $0 or the result of the following computation: [Homestead Owner's Property Tax - (0.10 * Homestead Owner's 3-Year Average Gross Income)]. The gross income measure used in computing the credit is the Federal Gross Income. The 3-year average is based on the three years prior to the year immediately preceding the year that the credit is to be obtained.

It is estimated that the amount of credits claimed for Pay 2007 and Pay 2008 taxes could potentially total about $102 M each year. From that point, credits claimed could potentially decline by about 0.3% annually provided income growth exceeds property tax growth as currently projected. The estimate of annual property tax credits is based on simulations utilizing the homeowner's property tax deduction and Federal AGI data from tax year 2002 state income tax returns. Federal Gross Income is imputed from Federal AGI based on the relationship between these two measures in recent years. The 2002 income levels are estimated for subsequent years through 2010 based on forecast growth in Indiana Nonfarm Personal Income and in net property tax rates on homesteads.

Effect on Property Tax Revenue: A property tax credit that is not funded from some other revenue source normally causes a revenue loss for local taxing units. However, the bill directs local officials and the DLGF to adjust the assessed value (AV) that is used in setting tax rates in order to eliminate or minimize the effect of the credits on local units. This means that for levy-controlled funds, the AV used to calculate tax rates will be artificially low and the resulting tax rate will be artificially high. The higher tax rate will be applied to the AV of all properties, both real and personal, and will produce a higher charged (abstract) levy for each unit. The higher abstract levies would result in increased PTRC and homestead credits. After all credits, including the credit created in this bill, are paid to homeowners, the taxing units' total revenues for rate-controlled funds should be relatively unaffected by this bill.

There would most likely be a reduction of revenue for local taxing units' rate-controlled funds such as cumulative building and capital projects funds. The revenue loss stems from the fact that the tax rate, if it is already at the maximum rate allowed, cannot be increased even if the assessed value is lowered.

Overall, about $30 M of the $102 M credit would be shifted to the state in the form of higher PTRC and homestead credits and the majority of the remaining $72 M credit will be shifted from homeowners to all property owners. The remainder would be lost revenue in the rate-controlled funds.

State Agencies Affected: Department of Local Government Finance.

Local Agencies Affected: County auditor; Local civil taxing units and school corporations.

Information Sources: OFMA Income Tax databases, 2000-2002. Economic Forecast Committee, *Nominal Nonfarm Indiana Personal Income and U. S. Personal Income*, December 14, 2004.

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